FOREIGN DIRECT INVESTMENT
IN SERVICE SECTOR IN VIETNAM

By

CHU Long Tuan

THESIS

Submitted to
KDI School of Public Policy and Management
in partial fulfillment of the requirements
for the degree of

MASTER OF PUBLIC POLICY

2011

FOREIGN DIRECT INVESTMENT
IN SERVICE SECTOR IN VIETNAM

By

CHU Long Tuan

THESIS

Submitted to
KDI School of Public Policy and Management
in partial fulfillment of the requirements
for the degree of

MASTER OF PUBLIC POLICY

2011

Professor Seung – Joo Lee

FOREIGN DIRECT INVESTMENT

IN SERVICE SECTOR IN VIETNAM

By

CHU Long Tuan

THESIS

Submitted to
KDI School of Public Policy and Management
in partial fulfillment of the requirements
for the degree of

MASTER OF PUBLIC POLICY

Committee in charge:

Professor Lee Seung – Joo, Supervisor

Professor Cho, Seong-Ho

Professor Kang, Younguk

Approval as of July , 2011

ABSTRACT

FOREIGN DIRECT INVESTMENT
IN SERVICE SECTOR IN VIETNAM

By

Chu Tuan Long

Vietnam has been considered a successful case over the last decade in attracting significant foreign direct investment inflows. The foreign-invested sector is now an important element of the corporate community in Vietnam, and an equally important engine of economic growth for the country. Thank to investment policy amendment, Vietnam has continuously seen FDI in its region increase sharply. Vietnamese government also gives top priority to utilizing FDI to develop service sector. However, the situation of slow growing service regardless of advantages is posing challenge for this country’s policy makers. The paper is designed to analyze and assess the situation of FDI attraction in service sector in Vietnam especially after Vietnam became a WTO member. Based on achievements and shortcomings, suggestions and measures to attract more FDI are discussed to find out most appropriate policy for service development in Vietnam.

ACKNOWLEDGEMENT

I would like to thank all people those have been with me and helped me finish the master's thesis.

First, I would like to convey my honest gratitude to Prof. Lee Seong – Joo for the helpful, effective and incessant support of my master study, for his enthusiasm and profound knowledge. His continuous energy and serious attitude in research have motivated me. Moreover, he is always accessible and shows willingness to help his students. I could not have imagined having a better advisor for my master study.

It is my honor to cooperate with Prof. Cho Seong – Ho by having him as my co-advisor. His broad knowledge into FDI astonishes me and inspired me to continue my thesis topic on FDI.

My sincere thanks also goes to Huong, Toan, Le Yen, Van, Dam Yen, Thao, Duc for sharing me with studying experience, materials, data and memorable moments in Korea.

Last but not least, I would like to express my deep and sincere gratitude to my family for their everlasting love and encouragement throughout my life.

TABLE OF CONTENTS

LIST OF TABLES

LIST OF FIGURES

LIST OF ABBREVIATIONS

FDI	**Foreign Direct Investment**
M & A	**Mergers and Acquisition**
WTO	**World Trade Organization**
UN	**United Nations**
OECD	**Organization of Economic Cooperation and Development**
TNCs	**Trans National Corporations**
R & D	**Research and Development**
AFTA	**ASEAN Free Trade Area**
AIA	**ASEAN Investment Area**
BTA	**Bilateral Trade Agreement**
IPR	**Intellectual Property Rights**
BCC	**Business Cooperation Contract**
BTO	**Build – Transfer – Operate**
BOT	**Build – Operate – Transfer**
BT	**Build – Transfer**

CHAPTER I: INTRODUCTION

1. The necessity of research

Since the Law of foreign investment was promulgated in Dec 1987, the foreign investment has played an essential role in altering Vietnam's economy in a prompt and stable way and help Vietnam gain a stride on its process of industrialization and modernization. Vietnam has witnessed during its transition to the market oriented economy two important developments. Vietnam's international trade has increased substantially and Vietnam has managed to attract a large inflow of inward FDI during the last two decades. These two developments have been considered as important source of economic growth of Vietnam (Le Dang Doanh, 2002).

Recent researches show that the achievement of Vietnam in attracting FDI inflow is much impressive. Vietnam has overtaken Indonesia, Malaysia, Thailand to become the FDI largest recipient in the ASEAN. With its participation in the WTO, Vietnam has endeavored to prove its worth in the world biggest playing field of trade. More and more international corporations see Vietnam a springboard to control the ASEAN market and have made huge direct investment in Vietnam.

For a nation on its way of developing economy from scratch after wars, FDI is manifestly among most key factors. Perceiving its importance, Vietnamese government has amended numerous relating regulations aimed at making Vietnam more attractive to foreign investors. This attempt has initially worked. However, in Vietnam, service sector has only contributed to roughly 30% of its GDP, much less than 70% of GDP that accounts for in a developed country. Vietnam's goal is to basically become an industrialized nation in 2020 in which service sector makes up a major part in the economy structure.

In fact, FDI in service sector has increased for recent years. Still, this rise does not match with Vietnam's potential in developing services. Since service development is among criteria to assess one's economy development, a weak service sector with its shortcomings is likely to reduce Vietnam competitiveness. Hence, FDI promotion in an effective way in order to develop service in Vietnam turns to be a key question.

2. Scope of research

The research analyzes the situation of FDI attraction in service sector in Vietnam during past years. Vietnamese government's moves from 2003 to present in facilitating foreign investors in service sector are focused. Service sector is also classified into different categories and the research focuses on main categories such as: Transportation, accommodation and food, finance and banking, education, health, construction, real estate and rental.

3. Methodology

Recall the basic concept and approach to FDI, service sector as well as elaborate the necessity of FDI attraction in service sector

Based on collected statistics and data to analyze the situation of FDI attraction in service sector in Vietnam; evaluate the advantages, disadvantages and drawbacks; point out fundamental challenges in recent years.

Based on achievement, shortcomings and forecast on future international context, measures shall be suggested and discussed.

4. Thesis structure

The thesis is organized as follows:

Chapter I: Introduction

Chapter II: Background

Chapter III: Situation of foreign direct investment attraction in service sector in Vietnam during past years

Chapter IV: Measures to promote foreign direct investment attraction in service sector in Vietnam next years

Chapter V: Conclusion

CHAPTER II: BACKGROUND

I. Literature review on FDI

1. Concept of FDI

Foreign direct investment is investment of foreign assets into domestic structures, equipment, and organizations excluding foreign investment into the stock markets. In its classic definition, foreign direct investment is defined as a company from one country making a physical investment into building a factory in another country. The direct investment in buildings, machinery and equipment is in contrast with making a portfolio investment, which is considered an indirect investment. In recent years, given rapid growth and change in global investment patterns, the definition has been broadened to include the acquisition of a lasting management interest in a company or enterprise outside the investing firm's home country. As such, it may take many forms, such as a direct acquisition of a foreign firm, construction of a facility, or investment in a joint venture or strategic alliance with a local firm with attendant input of technology, licensing of intellectual property (Jeffrey P. Graham and R. Barry Spaulding, 2005). In comparison with investments in the equity, foreign direct investment is considered to be more useful to host country. Equity investments are usually seen as "hot money" and tend to leave as soon as signs of trouble occur.

In Vietnam, foreign direct investment is construed to bring capital to Vietnam in the form of cash or any assets by foreign investors for the purpose of conducting investment activities (Law of Foreign Direct Investment).

2. FDI impact on the economic growth

Interested financial experts and researchers from international organizations and countries all over the world have more and more acknowledged the substantial impact of foreign capital to economic growth. FDI has become an essential form of international capital flow given dynamic age of globalization, liberalization and privatization. In World Development Report issued by World Bank in 2005, the magnitude of foreign capital flow to the recipient country economy was discussed in detail as recognition of the importance of no border investment.

Since FDI contributes to the new technologies transfer as well as capital accumulation to the recipient country, it may directly affect economic growth. In addition, Thank to direct transfer of technology, knowledge in the recipient country is augmented via organizational arrangements, new management practices, labor training and skill acquisition. As a result, economic growth is enhanced indirectly.

In emerging economies, FDI has played a crucial part in promoting economic growth and the standard of living. A positive correlation between economic development and FDI inflows has been shown in recent researches, provided that a minimum level of technological and infrastructure, educational development reached by the recipient countries.

A number of empirical studies on the role of FDI in host countries suggest that FDI is an important source of capital and complements domestic private investment, and is usually associated with new job opportunities and increases technology transfer, boosting overall economic growth in host countries. The relationship between growing FDI stock and economic growth has motivated a voluminous empirical literature in developed and developing countries. Asheghian and others confirm the existence of a positive and significant relationship between FDI and the economic growth in the United States (Asheghian, 2004).

However, negative effect on the recipient economy growth may be created by FDI if considerable reverse flows (remittances of profits and dividends) or concessions from the host country happen. Only when the host country could take advantage of FDI spillovers, its economic growth is fostered positively and effectively by FDI.

3. FDI in-flow into Vietnam

Between the 1980s and early 1990s, FDI flow into Vietnam was negligible with recorded only 213 million US dollars in 1991. However, the number of registered FDI has rocketed since 1992, reaching a peak in 1996 with recorded USD 8.6 billion. There are some reasons to explain this strong increase. A potentially untapped economy with a great market of 80 million people attracted foreign investors. Besides, a series of other positive factors such as high literacy rate, cheap labor cost and abundant labor force was taken into account.

Adding to such internal factors, there were some external ones accounting for the FDI inflow increase. The first was the trend of investing in developing countries between the 1980s and early 1990s. The South East Asia clearly benefited from this when becoming a key FDI recipient. In 1990, this area accounted for 37% the total FDI invested in emerging markets. The second was investor expectation of great profit from the transitional economies of former socialist sector where abundant business opportunities could be seen. Thirdly, stronger economies in the region as Malaysia, Singapore, Thailand have started to export capital.

Between 1991 and 1996, FDI played an important role in funding current account deficit of Vietnam and contributed considerably to the country's balance of international payment.

From 1997-1999, the Asian financial crisis resulted in a downfall of registered FDI in Vietnam, particularly 48% in 1997 and 58% in 1999. Vietnam saw its five major investors, all from Asia be busy with difficulties and challenges in their own countries. These investors had no choice but to postpone or cancel overseas projects to survive from the crisis. Expansion criteria into Asian market were also lowered which brought about the currency devaluation of South East Asian countries. When Vietnames Dong got weaker, Vietnam became less attractive to export-oriented projects.

From 2000, Vietnam has seen its value of registered FDI climb again.

II. Literature review on service sector

The service sector is one of the three economic sectors, the others being the manufacturing and the agriculture, fishing, and extraction. "Soft" parts of the economy belong to the service sector. For example, people apply their time and knowledge to improve potential, performance and productivity. The production of services instead of end products is the fundamental service sector's characteristic. Services can be regarded as intangible goods including discussion, experience, advice and attention.

The service sector gets involved with the provision of services to other businesses as well as final consumers. Goods are transported and distributed from producer to a consumer involve services. In the process of supplying services, the goods may be transformed. However, interaction among people rather than physical goods transformation is focused.

For recent years, a significant shift from the primary and secondary sectors to the service sector in developed countries has been recorded. In the Western world, the service sector becomes the biggest and also the fastest-growing sector of the economy.

III. The necessity of attracting more FDI in service sector

25 years since 1986 DOI MOI (innovation), Vietnam sees its all economic sectors developing strongly and dynamically. Service sector in this trend has also shown its rapid progress. However, the growth is considered not to live up to its potential.

Before DOI MOI, Vietnam had clung to the centrally planned economy in which service sector was restricted to distribution, circulation and was managed by State. Modern services were absent and/or prohibited. By shifting from centrally planned economy to Socialist-oriented market economy, service sector has been encouraged to expand. The diversification of services is the breakthrough which helps the economy to operate more effectively.

Between 1986 and 1996, the growth rate of service sector was always higher than that of economy. Nonetheless, the service sector's growth rate had slowed down since 1996 and could not reach its target set in Five year socio-economic development plans. Even the rate has shown a recovery in recent years, it is still far beyond the economic growth rate.

Between 2000 and 2005, only few services have their growth rates surpassed GDP growth rate. In general, services with high growth rate usually account for a small proportion of GDP while services contributing most to GDP have grown at a snail's pace. Hence, it is necessary to attract FDI in service sector because of the following reasons:

Firstly, service sector has shown more and more significant contribution to GDP and has fostered the transition of economic structure. Service is the economic sector which is most capable of mobilizing capital, associating and promoting all economic sources in order to create surplus value. Service sector itself also contributes considerably to making additional value. Besides, in the context of slowing down manufacturing all over the world, strong development of service sector helps to establish a more effective and dynamic economy. In Vietnam, there are numerous opportunities for underdeveloped services to expand. Hence, exploiting service sector's potential is the best way to promote the economic growth.

Secondly, service sector plays an important part in improving other sectors effectiveness. In process of international economic integration and market economy development, Vietnam faces the increasing demand of commodity manufacturing and consumption. As a result, service sector development becomes the core issue for policy makers. Services such as transportation, communications, commerce, finance and banking on the one hand contribute directly to service sector growth, on the other hand stimulate and facilitate other sectors to develop. Especially, high-level services namely information technology, education and training, communications assist manufacturing significantly by improving input quality and effectiveness of manufacturing process as well. In fact, along with economic development, skilled labor and scientific advance have been key factors for both agriculture sector and manufacturing sector.

Thirdly, service sector development contributes importantly to dealing with social problems by creating jobs, raising income and living standard, and improving environmental condition. Service sector has attracted more and more labors from other sectors in company with its progress. The increase has resulted from the fact that the number of agricultural and fishing job is in decline trend. The transfer between the two economic sectors helps to reduce the income gap.

Besides, services such as public administration or public transportation which are mainly provided by government give top priority to offering equality. In another word, services development has positive impacts on ensuring and upholding democracy and social equality.

Moreover, services affect environment in an active and positive way. Service itself is deemed to be a “pure” or “non-smoke” industry and hence minimizes the environmental pollution. Some services, for instance ecotourism and environmental sanitation, even improve environment.

Fourthly, attracting FDI aims to develop high level services. In developed countries, high level services play an essential role in economy and investment in high level services has become a natural tendency. However, in case of Vietnam, high level services have been ignored for a long time and their sluggish growth has contributed unremarkably to GDP. Due to strict requirement on technology and capital, it is necessary for Vietnam to rely on FDI to develop its high level services.

CHAPTER III: SITUATION OF FDI ATTRACTION IN SERVICE SECTOR IN VIETNAM DURING PAST YEARS

I. The Government’s efforts to attract FDI in service sector

The Government has shown its determination in improving the investment climate by issuing the Investment Law and the Enterprise Law (taking effect from July 1st 2006) in the direction of:

+ Increasing the business autonomy (in selecting investment partners, the form of investment, the investment fields...) as well as equal access to investment resources and to public services.

+ Removing investment barriers (the localization rate, export and import quota).

+ Diversifying the forms of investment: merger and acquisition (M & A), capital contribution for share purchase, business investment and development are stipulated adding to the forms of business cooperation contracts, joint venture and 100% foreign investment as before.

+ Reforming investment procedures by strongly expanding the decentralization of the investment certificates grant and state management over investment activities; the verification procedures are simplified.

Besides, many laws which have been issued recently such as the Technology Transfer Law, Law on Real estate business, Law on Credit Institutions, , , etc. favor foreign investors directly or indirectly in the market of science and technology, real estate market and capital market in Vietnam.

The reforming process is beefed up in order to reduce the state monopoly and also to facilitate all the economic sectors. Particularly, foreign investors are facilitated to directly participate in the privatization or through the Stock Exchange.

Along with deeper economic integration into the world economies, especially after becoming a WTO's member and a non-permanent member of the 2008-2009 UN Security Council, Vietnam keeps on performing the liberalization process following the international committed route as follows:

+ Ceiling for the whole tariff has been bound of about 10,600 lines and taxes have been cut from 16.9% down to 14.1% since January 1st 2007. Commitment to take part in some or all of a number of agreements liberalizing the sector for construction equipment, aircraft equipment, textiles, information technology products... was also made.

+ 11 out of 12 service industries are committed to being subject to open, many of those are essential sectors such as education, banking, healthcare, insurance and telecommunications.

+ Also, Vietnam is committed to conforming to most of the required obligations in the WTO multilateral agreements right after joining WTO. Moreover, the WTO requirements on transparency (law formation and enforcement process, procedures for licensing) are committed to implementing.

Given new conditions, in order to meet the development requirements, all resources are mobilized to develop the infrastructure. At the same time, the administrative reform program has been launched by the Government, a breakthrough to improve the state management efficiency. Also, the management decentralization of state budgets and investment for provinces, ministries is furthered, the mode of service, training and retraining staff and public officials are enhanced.

Vietnam has always attached special importance to services during past years. In 2004, the Prime Minister issued the instruction 49/2004/CT-TTg dated Dec 24 on service development in the five-year plan of 2006-1010 which concretized Vietnam's efforts in promoting this sector. The instruction specified the following priorities:

Promote services which can yield foreign currency revenue such as tourism, finance and banking, communication, transportation, logistics.

Speed up FDI attraction to develop high level services, for instance education, health and culture.

Survey and assess competitiveness of each service, determine which ones need to be protected and which ones are open. Set up incentives for foreign investors in specific services

In addition, FDI promotion division was established belonging to Ministry of Planning and Investment in 2003. The division in association with the Chamber of Commerce and Industry has endeavored to promote investment in services. The measures which are usually taken include: enlist the need-to-invest projects, take place seminar or workshop on investment, publish bulletin or handbook for concerned investors, associate with FDI enterprises in attracting potential investors.

The government has also issued regulations on FDI promotion in service sector in order to ensure the consistency between the center programs and the local programs conclude. Besides, multilateral and bilateral negotiations have been paid special attention aimed at facilitating foreign investors. So far, Vietnam has concluded investment promotion agreements with 46 nations over the world.

Vietnam's efforts has contributed to the increase of the number of projects as well as the total capital over years

Table 1. FDI in service sector in the period of 1988-2007

Year	The number of projects	The total capital
1988	6	49,7
1989	15	215,8
1990	23	236,8
1991	42	496,6
1992	51	578,8
1993	67	1.322
1994	83	1.500
1995	80	1.532
1996	72	4.825
1997	73	2.371
1998	68	1.215
1999	61	551
2000	42	255
2001	85	586
2002	96	519
2003	99	474
2004	132	876,8
2005	196	1.763
2006	243	3.809
2007	402	6.009
Total	**1.936**	**29.193**

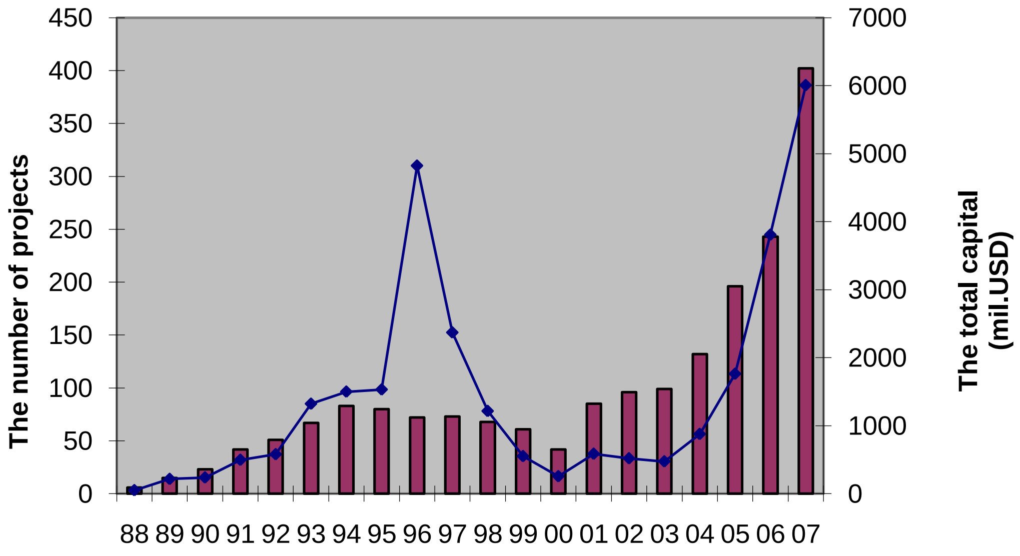

Figure 1. FDI in service sector in the period of 1988-2007

The change has reflected Vietnam's attempt consistent with the world context. The number of projects and the total capital rose gradually between 1990 and 1994 before sharply soared in 1995 thanks to investment promotion measures. However, due to the 1997 financial crisis, Vietnam saw its FDI flow into services dropped significantly. The flow only recovered since 2006 resulted from more effective investment policy and wider openness on services. Moreover, becoming a WTO's member since 2006 has accounted for a more competitive investment environment and has made Vietnam more attractive in the foreigner's eyes.

II. FDI in service by sub sectors

In fact, there are 7 main sub sectors that have contributed most to FDI attraction in service including: Transportation - communication, hotel and tourism, finance and banking, culture - health – education, new urban area construction, building construction, and industrial area construction

Table 2. FDI in service sector by sub-sectors

Ordinal No.	Sub-sector	Number of projects	Total capital (mil. USD)
1	Transportation - communication	232	5.342
2	Hotel - tourism	318	7.911
3	Finance - banking	76	931,5
4	Culture - health – education	290	1.039
5	Industrial area construction	30	1.184
6	New urban area construction	10	3.475
7	Building construction	175	7.986
8	Other services	805	1.322
Total		1936	29,193

Among sub-sectors, hotel - tourism and building construction have contributed most to FDI in service with the total capital of approximate 8 billion dollars each, followed by rough 5.3 billion dollars of transportation – communication. It is no surprise since there has been a boom in establishing representative offices and factories from multinational corporations in recent years. The increasing demand on leasing office helps draw FDI inflow into these sub-sectors. The demand is forecasted to rise continuously hence these sub-sectors are still playing as motive force in FDI attraction in service next years.

However, finance-banking with only 76 projects and almost 1 billion dollars has not yet reached its potential while, in developed economy, it always plays the most important role in service sector. It is clear that Vietnam has a great deal of work to do to improve this key sub-sector.

In recent 5 years (2003-2007), the investment trend has stayed the same as the 7 above sub-sectors still account for most FDI in service sector. Hotel - tourism along with building construction assures of the first place in FDI attraction when the total capital has grown regularly over years before reaching its peak of 1.5 billion dollars (130 projects) in 2007. At the same time, building construction became the fastest growing sub-sector. In 2003, there were only 2 projects valued 58 million dollars in building construction. However, the number of project increased sharply to 46 with the total capital of 2.5 billion dollars at the end of 2007.

Sub-sector	2003		2004		2005		2006		2007	
	No. of project	Total capital	No. of project	Total capital	No. of project	Total capital	No. of project	Total capital	No. of project	Total capital
Transportation - communication	16	52,800	37	182,150	42	193,600	43	901,818	86	578,731
Hotel - tourism	27	188,800	31	185,350	29	65,340	52	1,131,145	130	1,485,930
Finance - banking	6	3,530	5	81,150	7	68,900	5	32,900	1	20,000
Culture - health – education	37	95,200	46	222,510	45	226,400	47	189,930	65	221,332
New urban area construction	0	-	0	-	1	463,280	2	526,090	4	672,860
Building construction	2	58,000	4	132,060	16	381,057	37	673,565	46	2,482,640
Industrial area construction	2	21,900	1	6,200	2	8,500	5	56,175	9	326,755
Other services	9	53,940	8	67,420	54	356,226	52	298,082	61	220,866
Total	99	474,170	132	876,840	196	1,763,303	243	3,809,705	402	6,009,114

Table 3. FDI in service sector by sub-sectors between 2003 and 2007

III. FDI in service sector by region

Foreign investment can be found in 63 provinces and cities nationwide, of which Ho Chi Minh city still attracts the most foreign investors with 836 valid projects and the registered capital of US$10.5 billion, accounting for 43% of the total projects and 36% of the total registered capital of the country. Following is Ha Noi with US$8.5 billion registered capital, accounting for 29% of the total registered capital of the country. Next come Ba Ria – Vung Tau, Da Nang, Hai Phong.

In terms of the larger region, the Southeast region with four provinces and cities is always in the top 10 provinces to attract foreign investment with 61% of the total projects and 52.7% of the total registered capital of the nation. Following is the Red River Delta headed by Hanoi occupying 24.6% of the total projects and 18.3% of the total registered capital of the country. The Northwest is the least foreign investment attraction, only accounting for 0.4% of the projects and 0.1% of the total registered capital.

Table 4. FDI in service sector by region

Ordinal No.	Location	No. of project	Total capital
1	Ho Chi Minh city	836	10.563
2	Ha Noi	462	8.482
3	Ba Ria – Vung Tau	80	2.209
4	Da Nang	48	1.329
5	Hai Phong	78	1.001
6	Lam Dong	11	895
7	Binh Duong	62	651,2
8	Thua Thien Hue	21	595,6

9	Long An	15	580,9
10	Quang Ninh	51	478
11	Dong Nai	29	339,9
12	Binh Dinh	11	301,6
13	Quang Nam	17	289,1
14	Binh Thuan	30	182,7
15	Others	186	1291,6
Total		1936	29.193

IV. FDI in service sector by investors

45 nations and territories have invested in Vietnam with the largest being the Singapore with the total registered capital of US$7.6 billion accounting for 26% of the total foreign investment in Vietnam, South Korea rakings the second with US$5.3 billion or 18% of the total, followed by British Virgin Islands with US$3.8 billion, occupying 13%; Hong Kong ranks the fourth with US$2.9 billion, accounting for 10% of the total registered foreign investment.

Table 5. FDI in service sector by investors

Ordinal No.	Nation	No. of project	Total capital ($ mil.)
1	Singapore	280	7.589
2	South Korea	332	5.361
3	British Virgin Islands	128	3.830
4	Hong Kong	236	2.896

5	Japan	250	1.724
6	Taiwan	132	1.680
7	France	105	1.462
8	US	114	1.420
9	Luxembourg	8	788,2
10	Australia	73	756,8
11	Others	278	1.684
Total		1936	29.193

Vietnam is apparent to depend on main investors when the top ten countries alone contribute to 94% of the total capital. Some countries such as South Africa and Mexico claim for 1 project only with less than US$1 million but pave the way for attracting more FDI from potential areas like Africa and North America region.

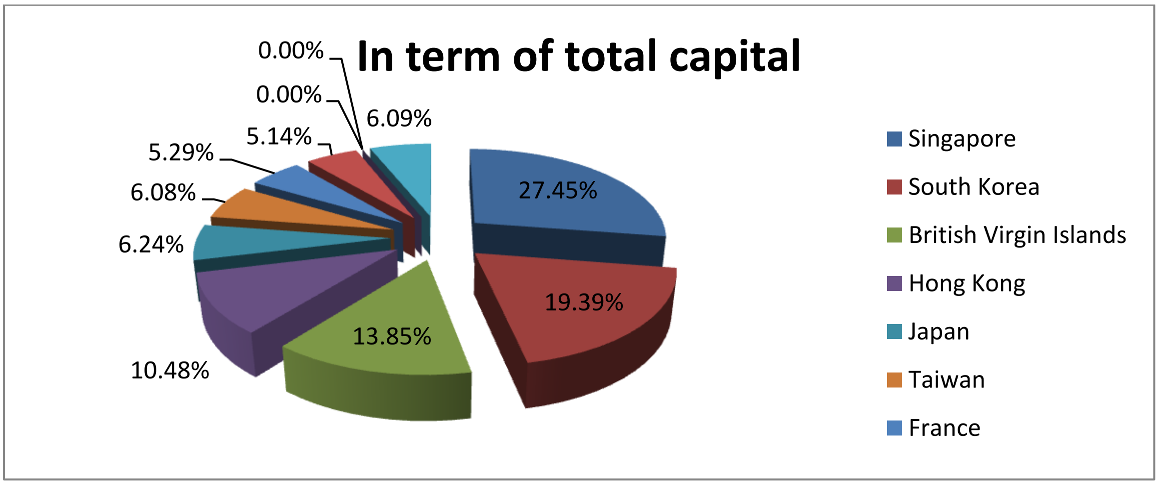

Figure 2. FDI in service sector by investors in term of total capital

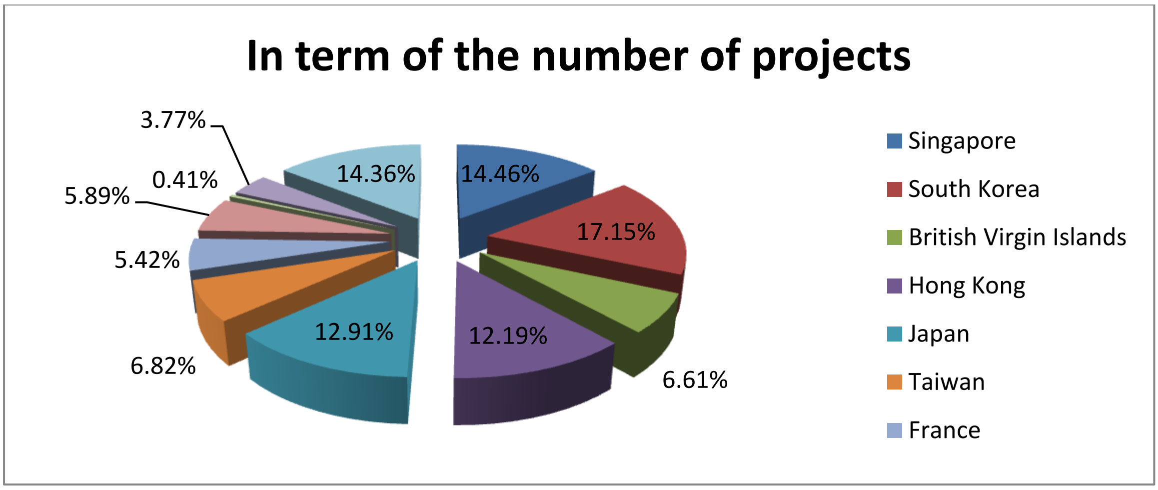

Figure 3. FDI in service sector by investors in term of number of projects

V. FDI in service sector by investment form

So far, there have been 6 forms of direct investment in Vietnam. In the early days of economic reform, a strong preference for FDI in 100% foreign owned was given by the Government, up to 1999, this form accounted for the majority of projects each year. However, the trend has shifted as joint-venture form has increased over time. In 2009, the total capital under this form even was greater than all other forms put together.

The latest form is the parent-affiliates claiming for 0.4% of the total capital only. The form is forecasted to make a great stride in the future since it is increasingly preferred by the foreign investors.

Table 6. FDI in service sector by investment form

Ordinal No.	Form of investment	Number of project	%	Total capital	%
1	100% foreign owned	964	49,79	8.964	30,71
2	Joint-venture	830	42,87	16.143	55,3

3	BCC	122	6,3	2.920	10
4	BOT, BTO, BT	1	0,05	619	2,12
5	Joint stock	18	0,93	447,6	1,53
6	Parent-affiliates	1	0,05	98,4	0,34
Total		1.936	100	29.193	100

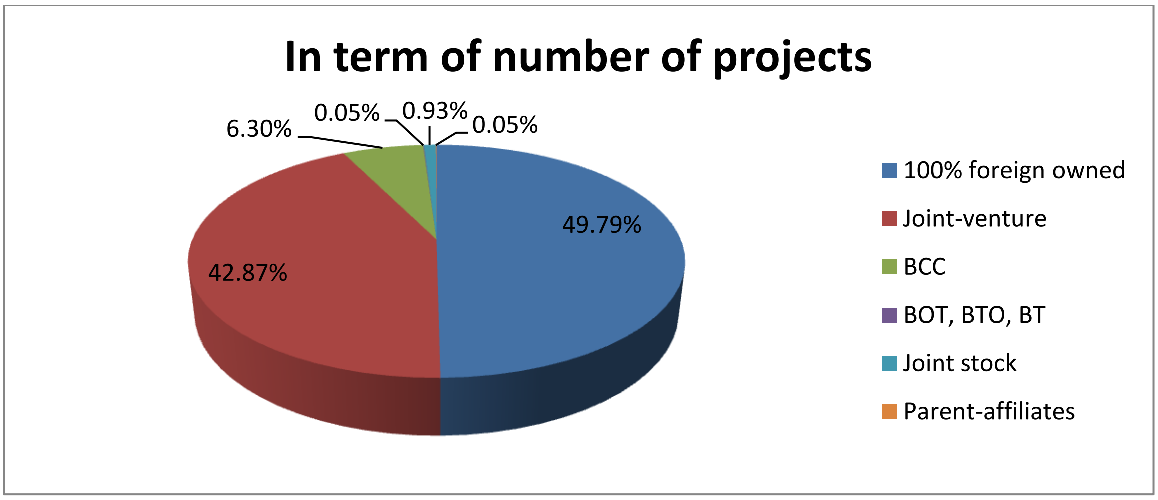

Figure 4. FDI in service sector by investment form in term of number of projects

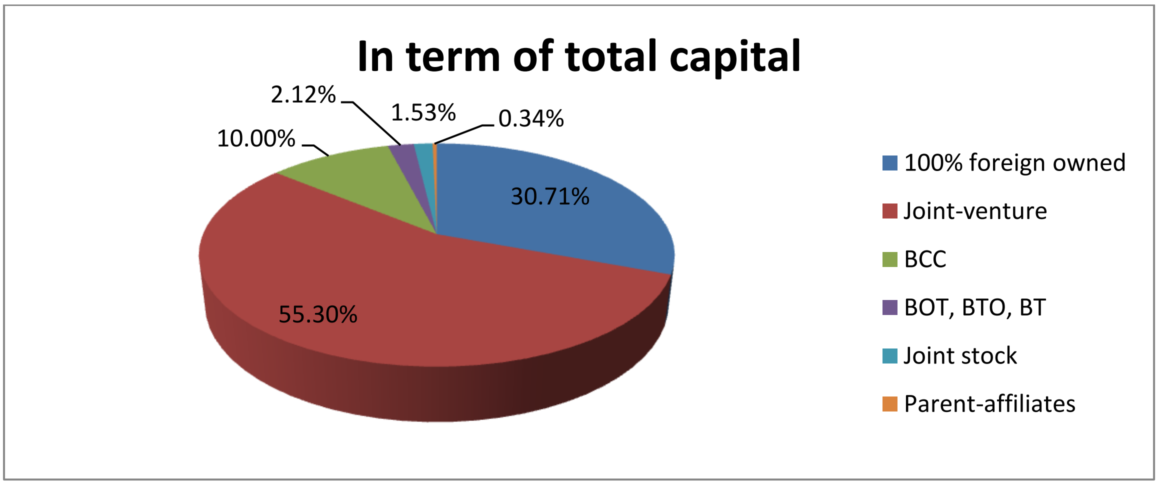

Figure 5. FDI in service sector by investment form in term of total capital

VI. Assess situation of FDI attraction in service sector in Vietnam

1. Achievements

A sharp increase of FDI in service sector has been recorded in recent years. In 2005, there were 196 projects with the total capital of US$1.7 billion. The number of projects and the total capital climbed to 243 and US$3.8 billion respectively in 2006 before reaching a peak of 402 and US$6 billion in 2007. Besides, the proportion of above-US$100 million projects has made a rapid growth in which real estate – related projects are overwhelming.

FDI in main sub – sectors of services contributes remarkably to the national industrialization and modernization process and brings about positive impact on social economics as follows:

Help to foster the economic transition consistent with the national development strategies. FDI in service sector has risen regularly over years and soared to US$ 40 billion or 55% equivalent of the total FDI in the country as of the first half of 2010.

Help to improve the infra – structure capacity by developing transport and communication services and hence improve the investment environment.

Thank to advanced technology, products and services from FDI projects become more competitive in the international market and therefore pave the way for traditional services to step up export

Contribute to job creation and income raise for local labor. Until 2009, FDI in service sector has helped to create more than 50,000 direct jobs and thousands of indirect jobs. Labor in service sector accounts for 25.3% of the total work force compared with 56.8% and 17.9% in agriculture sector and manufacturing sector correspondingly and has a voice in alleviating the tense situation of job shortage. Labor income in FDI projects in service sector is often more attractive and stable and in return, high skill is required. As a result, labors are encouraged to enhance knowledge and proficiency to receive higher remuneration. Moreover, when being recruited as managers in FDI projects, local labors gain valuable experience in management and improve their qualifications.

Along with the escalation of the number of projects and the total capital, financial scale of projects has gone up marked by the presence of above – US$1 billion projects. The thing is foreign investors belief has been shown as they ever more tend to implement large – scale projects.

2. Shortcomings

Even though FDI inflow into service sector has been reported to rise gradually over years and promote the economic transition, the progress is still slower than expected. Services usually account for 70% of the total GDP in developed countries, but the corresponding figure in Vietnam in turn is 38.2% in 2003, 38.4% in 2004, 38.7% in 2005, 38.8% in 2007, and roughly 40% in 2009. In fact, whereas the growth rate of main sub – sectors is 10%, the overall growth rate of services is around 6%, lower than the GDP growth rate. Prominent shortcomings in FDI attraction in service sector include:

FDI inflow into sub – sectors is imbalanced. Government's efforts in backing for services such as ship repair, seaport logistics and maritime transport aimed at collection foreign currency have not been repaid. FDI in these services makes no headway regardless of continuous investment incentives. Due to the lack of qualified intermediate ports as well as deep - water ports which can receive more than 500,000 dead weight tonnage ships, the unavailability of modern loading and unloading technology, seaport service potential has been restricted. On the contrary, FDI in Hotel – tourism and Building construction have made an impressive growth.

FDI in Finance – banking has not reached its potential. In fact, both the number of projects and the total capital in this service are much lower than other main sub – sectors and make a sluggish progress over years. Many financial services which are prevalent and popular in the world become brand new in Vietnam. The infant stock market taking its first steps in the absence of transparency and professional management has not yet served as a useful capital mobilization channel. The necessary reforms in bank system in order to reorganize financial market effectively have not been seen.

FDI projects in Building construction are in slow progress that have made negative influences on FDI inflow. The sub – sector has flourished during past years and hit the climax in 2007. However, the sluggish progress not only affects negatively the effectiveness of the sub – sector but also restricts FDI inflow into other sub – sectors. Most of investors find it difficult in implementing site clearance. Big compensation and long schedule are likely to increase the initial expenses and frustrate the investors. These shortcomings are attributed to ambiguous regulations and complicated administrative formalities.

Unhealthy competition among localities regarding FDI attraction is recorded. Too much decentralization leads to fragmentation of the national economy as 63 provinces and cities in the whole nations are reckoned to act as 63 independent and competitive counties in FDI attraction.

CHAPTER IV: MEASURES TO PROMOTE FDI IN SERVICE SECTOR IN VIETNAM NEXT YEARS

I. The international context and affecting factors next years

Globalization and international economic integration have become the general trend over the world. Countries have actively integrated into international market through bilateral and multilateral agreements on trade liberalization and apprehensive domestic market openness. Trade and investment activities in every country are closely associated with international economic organizations.

The increasing trade liberalization trend has been confirmed and become prevalent during the first years of the 21st century. The step by step removal of tariff and non – tariff barriers to trade has facilitated the investment flows, paved the way for closer economic ties among nations and boosted the globalization process. However, beside obvious advantages on domestic economy, trade liberalization also exposes Vietnam to challenges in the pursuit of a strong and stable economy.

Competition in FDI attraction turns out to be more severe than ever. FDI has been recognized as an essential source in developing economy and improving growth rate in developing countries. Reform in regulations has been made, incentives for foreign investors have been offered, domestic market has been opened, these actions all aim to attract more FDI. Most developing countries rely on similar advantages such as low labor cost, available and abundant resources to attract FDI. Hence, apart from traditional advantages, favorable policies and attractive investment environment are required to improve the competitiveness.

Trans National Corporations (TNCs) more and more play an important role in FDI in-flow. TNCs provide capital for and transfer technology to developing countries. FDI inflow into these countries rose to US$1046 billion between 2001 and 2005 from the level of US$995 billion during the period of 1996 – 2000, mostly originated from TNCs. Besides, TNCs also play a key role in research and development (R & D) over the world. The 700 world biggest TNCs's R & D spending accounts for 98% of all TNCs's R & D spending and 70% of global R & D spending.

Vietnam has joined ASEAN Free Trade Area (AFTA) and ASEAN Investment Area (AIA) to boost direct investment within ASEAN and attract foreign investment into the area as well. Pursuant to relating agreements, tariffs are cut down over a period of time and investment policy is liberalized and open. As a result, investment climate in Vietnam is promoted and Vietnam stands much chance of attracting more FDI.

By becoming the WTO 150th member since January 11, 2007, Vietnam has committed to increasing market access for U.S. goods and services as well as ensuring transparency in regulatory trade practices. Simultaneously, there are commitments on services (foreign service providers have equal accesses), goods (less agricultural subsidies in form of ceilings, quotas, tariff), and on realizing agreements on anti-dumping and countervailing measures, sanitary and phytosanitary measures, investment measures, technical barriers to trade, intellectual property.

In addition to WTO, U.S investors have much benefited from the U.S - Vietnam Bilateral Trade Agreement (BTA). U.S. investment, services and goods are ensured fair access by WTO and the BTA. Records show that Vietnam overall fulfill its bilateral and international obligations, though remained concerns in some areas, such as intellectual property rights protection.

II. Measures to promote FDI in service sector in Vietnam

1. General measures to attract FDI

1.1. About investment insurance

The capital and assets need to be ensured: in no case the Government applies administrative measures that results in nationalization or confiscation of the investor's legitimate assets and investment capital (except in unavoidable cases for reasons of national security and defense where specific regulations are stipulated)

Protect Intellectual Property: the investor's legitimate interests in technology transfer in Vietnam or other intellectual property rights in investment activities shall be ensured in accordance with Intellectual Property Law and other legal provisions involved.

Trade-related investment and market to be opened: in reference to the provisions of international treaties to which Vietnam is a member.

Transfer assets and capital abroad: the legal funds, assets, capital, profits can be remitted abroad by investors after financial obligations to the State of Vietnam are fulfilled.

Apply appropriate charges, fees and prices: In the course of investment activities in Vietnam, uniformly appropriate charges, fees and rates for goods and services are applied to investors.

In case of changes in policies and laws, investment activities are still ensured.

1.2. About fields of investment preferences

Foreign direct investment plays an essential role in the Vietnam total social investment capital. It is necessary for the Government to issue policy aimed at promoting the capital flow of foreign direct investment and improving the foreign direct investment effectiveness and quality.

The foreign direct investment attraction is prioritized in the following sectors:

+ Ecological environment production; use of modern technology and science; production of information technology, biotechnology, hi-tech products and new materials.

+ Infrastructure such as urban areas, construction of infrastructure for industrial zones, electricity and water supplies, seaports, transport, , , etc; Besides, key projects are focused to create a breakthrough in the infrastructure system.

+ Human resources developing projects involved in training and health, sports , education and labor-intensive projects.

+ Investment projects in economic zones, hi-tech zones, export processing zones , industrial areas as well as investment in areas of socio-economic disadvantages.

1.3. About investment preferences

In each period, a series of incentives for investors and investment projects is applied aimed at attracting more investment into the regions and sectors, including:

Tax preferences:

+ The duration of tax exemption or reduction in accordance with the tax legislations, the duration of preferential tax rates, the preferential tax rates are enjoying by investors with projects being subject to investment preferences under the Law.

+ The corporate income tax: investors can enjoy the 10% or 20% preferential tax rates (normally 25%) from 10 to 20 years (even some life-long preferences projects); In addition, exemption of corporate income tax up to 4 years and 50% of corporate income tax up to 9 years after corporate income tax exemption is expired can be applied.

+ After the corporate income tax obligation is performed, tax preferences for income earned from purchase of shares and capital contribution can be enjoyed by investors in line with the tax legislation

+ Investors are exempted from import duties for transport vehicles, materials, equipment and other goods for the investment projects implementation in Vietnam in line with the Law on import and export tax.

+ Investors are exempted from income tax for income from technology transfer activities of projects subject to investment incentives.

Loss shifting:

Losses suffered by investors (certificated by the tax authorities) would be subject to transfer to the following year and would be deducted from taxable corporate income in reference to the Law on corporate income tax. The loss shifting duration must be within five years.

Depreciation of fixed assets:

Accelerated depreciation for fixed assets can be applied for business projects with efficiency or investment projects in the geographical area or field of investment incentives; the maximum of these rates could be twice the depreciation rate of fixed assets.

Preferences on land use:

Reduction or exemption of land use tax, land use fees and land rent can be enjoyed by investors in the areas and fields of investment incentives in line with the Law on land the Law on tax.

Incentives for investors in economic zones, hi-tech parks, export processing zones, industrial parks:

Preferential treatment to investors in economic zones, hi-tech parks, export processing zones, industrial parks shall be given by the Government based on the socio-economic development conditions in each period.

2. Measures to attract FDI in sub – sectors of service

Joining WTO along with market opening agreements has facilitated the development of services. However, each sub – sector has its own characteristics requiring specific strategies and consistent measures in order to maximize potential. Suggested measures include:

2.1. Remove restrictions on FDI into Hotel – tourism.

According to Vietnam's WTO commitments on services, Hotel – tourism has become more open. Still, foreign tour guide is forbidden that hampers the sub – sector's progress. Domestic tour guides often lack of experience on tour management as well as professional skills which can be learnt from foreign counterparts. Full openness of Hotel – tourism is considered to be a foundation to strongly develop services. Along with tourism services development, construction and/or upgrade of high level resorts, hotels should be implemented comprehensively and effectively. Investment promotion activities need more concerns in order to introduce world-widely the nation's potentials.

2.2. Reform bank system.

Financial and banking is among key sub – sectors which always maintains the annual growth rate higher than that of overall economy. However, in recent years, the sub – sector has its contribution to the nation's GDP slowed down. This outcome results from the Government's preference in finance, credit and tax for State owned enterprises. In addition, the infant commercial bank system is still developing in a small scale without sustainable strategies. The measure is to reform bank system absolutely in which high level human resource training is the center. The measure, in one hand, helps domestic banks become more competitive and, in the other hand, makes the bank system stable in order to cope with external changes. Moreover, privatization of State owned banks and call for strategic investors need to be furthered. The strategic investors are expected to help improve administration skill and build consistent long term plans.

2.3. Boost investment in education.

Most labor working in FDI projects are unskilled workers. Lack of domestic skilled workers results in recruitment of native or third party workers to manage and expedite projects. Hence, the project efficiency is reduced and investment climate become less competitive. In order to confront with the challenge, Vietnam must call for more direct investment in education aimed at developing educational infrastructure. One of feasible measures is to associate with prestigious universities all over the world. Relying on that, exchange programs are conducted to help domestic students become more active and well – prepared. Besides, the Government should pave the way for foreign universities to open new campus in Vietnam.

2.4. Speed up the progress of building construction projects.

One of obstacles is site clearance which is often sluggish and hampers the project progress. The time has come for the Government to set up a land reserve available for building construction projects. Another rising concern is urban planning which is deemed to be too general and short of synchrony. Discrepancy among plans is likely to increase investment cost, slow down project progress and frustrate investors. The Government must issue consistent and detailed plans to set investors mind at rest.

2.5. Remove the monopoly in providing public services.

Some services such as electricity and water still are protected by the Government and make foreign investors uninterested in making investment decision. Power outage is common and turns to be a significant threat to economy. Although foreign investors can freely participate in electricity projects, they have to share a common and unique consumer, Electricity of Vietnam (EVN), who possesses the whole electric transmission system. This is the crucial problem hindering FDI attraction in electricity projects. The Government can step by step remove the monopoly in providing public services to attract more FDI while the State management role is still ensured.

CHAPTER V: CONCLUSION

Vietnam has attracted successfully FDI inflows into its transitional, developing economy since a foreign investment law was first introduced in 1987. Indeed, over the last decade FDI has played a key role in the macro-economic development, business liberalization, economy transition and contributed to make the miraculous growth story of Vietnam. FDI, regarded as the "imported private sector" has created a strange wind across the country where its existing fledgling private sector did not work well at the beginning of the 1990s. Without the presence of FDI activities, it is difficult to imagine how DOI MOI (renovation) process would operate. Over past 20 years (1998 – 2009), FDI has accounted for 20% of GDP, created more than 810,000 jobs and provided economic sectors with capital to develop. Thank to FDI, service sector has a fast growth especially after WTO commitments come into force.

However, Vietnam should not be content with the debut success as the potential in service sector is still big and the competition from neighbors within South East Asia is rising. The strongly increasing capital demand for services also poses challenges for Vietnamese policy makers. The Government must continue to take appropriate measures to improve investment climate aimed at developing service sector and keeping the country an ideal destination for FDI.

REFERENCES

1. Nick J. Freeman, 2002. *Foreign Direct Investment in Cambodia, Laos and Vietnam: A Regional Overview*.
2. Athukorala, 2002. *Foreign Direct Investment and Manufacturing Exports: Opportunities and Strategies*
3. Binh, N. and J. Haughton, 2002. *Trade liberalization and foreign direct investment in Vietnam*. Suffolk University.
4. Freeman, N. and C. Nestor, 2002. *Re-thinking FDI in Vietnam: fuzzy figures and sentiment swings.*
5. Kokko, A., K. Kotoglou and A. Krohwinkel-Karlsson, 2003. *The implementation of FDI in Viet Nam: an analysis of the characteristics of failed projects*. Transnational Corporations.
6. Mirza Hafiz and Axele Giroud, 2004. *Regional Integration and Benefits from Foreign Direct Investment in ASEAN Countries: The Case of Vietnam.* Asian Development Economic Review.
7. Tran Van Tho, 2004. *Foreign Direct Investment and Development of Supporting Industries in Vietnam*. Annual Bulletin of the Institute for Industrial Research of Obirin University.
8. Le Thanh Thuy, 2005. *Technological spillovers from foreign direct investment: The case of Vietnam, mimeo*. Graduate School of Economics, University of Tokyo.
9. Nguyen Phi Lan, 2006. *Foreign Direct Investment in Vietnam: Impact on conomic Growth and Domestic Investment, mimeo*. Centre for Regulation and Market analysis, University of South Australia.

10. Nguyen Thanh Xuan and Yuqing Xing, 2006. *Foreign Direct Investment and Exports:The Experience of Vietnam*. Graduate School of International Relations, International University of Japan.

11. Nguyen Ngoc Anh, Nguyen Thang, 2007. *Foreign direct investment in Vietnam: An overview and analysis the determinants of spatial distribution across provinces*. University Library of Munich

12. My Hanh Hoang, 2008. *FDI in Vietnam: Towards Economic Growth for U.S. and Vietnam.*

13. Oxford Economics, 2009. *Country Briefings: Vietnam*

14. The World Trade Organization www.wto.org

15. Vietnam General Statistics Official www.gso.gov.vn

16. Vietnam Ministry of Planning and Investment www.mpi.gov.vn

17. Vietnam Chamber of Commerce and Industry www.vcci.com.vn